1984-85 ANNUAL FINANCIAL REVIEW

The Annual Report of the Supermarket Companies

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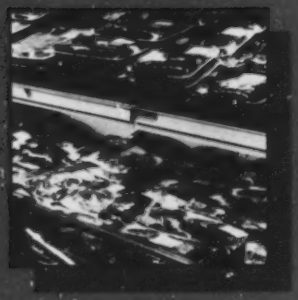

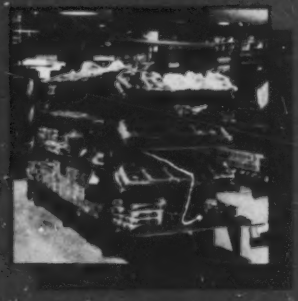

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FOOD MARKETING INSTITUTE®

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A NEW APPROACH

The Food Marketing Institute (FMI) has been tracking the financial performance of the supermarket industry for over a decade.

The *Annual Financial Review* (the *Review)* was designed to promote a better understanding of the economics of the supermarket industry. The economics of the industry has changed dramatically in the past 10 years.

In the past the *Review* was based on sales, assets, and liabilities of companies operating only supermarkets; however, today many firms are diversified enterprises operating more than just the traditional supermarket outlets.

Beginning with this report the *Review* will be based upon sales, assets, and liabilities of companies which operate supermarkets only or are primarily supermarket companies even though they may be diversified into other types of operations. To be considered a supermarket company at least 50 percent of the firm's sales must come from supermarket outlets. This approach to summarizing data for the *Review* will result in a report which more closely reflects the dynamics of the supermarket industry.

Many supermarket firms have fiscal years ending during the first quarter of the calendar year. Since the *Review* is now a supermarket company report the data are collected for fiscal years ending between April, 1984, and March, 1985.

For a historical perspective, financial data for 1984 were summarized with the traditional methodology used in prior years. This summary can be found in the Appendix.

The Food Marketing Institute (FMI) is a non-profit association that conducts programs in research, education and public affairs on behalf of its 1500 members—food retailers and wholesalers and their customers. FMI's domestic member companies operate more than 17,000 retail food stores with a combined annual sales volume of $130 billion—half of all grocery sales in the United States. More than three-fourths of the FMI membership is composed of independent supermarket operators or small regional firms. Its international membership includes more than 100 members from 40 nations.

EXECUTIVE SUMMARY

The Food Marketing Institute's *Annual Financial Review* provides a financial profile of supermarket companies in the United States.

This report provides the broadest and most representative sample of the industry available. Data were collected from 162 companies operating over 12,000 supermarkets.

The results of the *Review* indicate that average supermarket company profits increased in 1984/85 compared to the previous year. Net income as a percentage of sales was 1.15 percent in 1984/85 versus 1.01 percent in 1983/84.

On average, all sizes of companies showed an improvement in profitability during the past year. The larger companies showed a higher return on sales, whereas the smaller firms achieved a higher return on assets and net worth.

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FINANCIAL DATA AND RATIOS

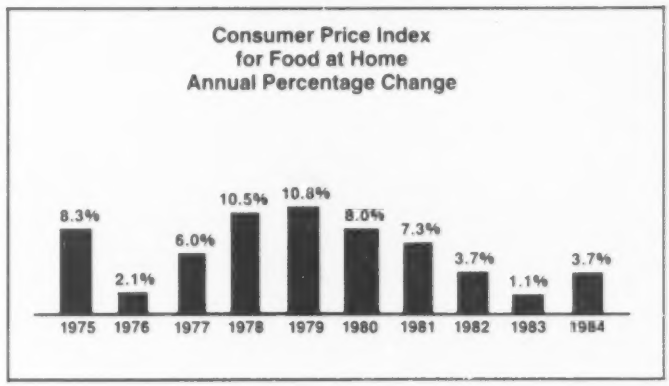
Selected Economic Data

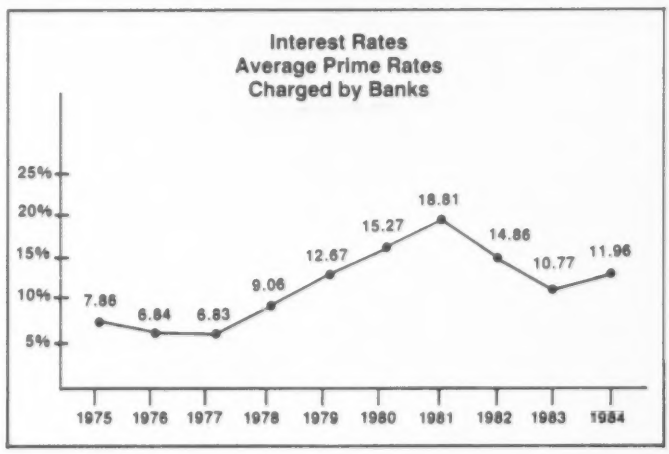
During 1984, the U.S. economy continued to recover from the most severe recession since the great depression.

Inflation, as measured by the consumer price index for all urban consumers, was 4.3 percent, a slight increase over 1983. The consumer price index for food-at-home rose 3.7 percent.

Interest rates dropped considerably during 1982, held steady through 1983 and increased slightly in 1984. The average monthly prime rate charged by banks in 1984 ranged from 13.0 percent to 11.0 percent.

With inflation at about four percent and the prime rate hovering around 12 percent, "real" interest rates in 1984 were considerably above historical levels.





Key Financial Ratios

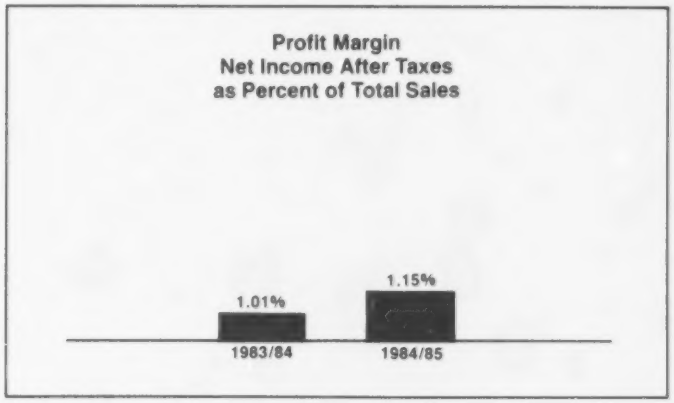
In measuring profitability, three financial ratios taken together provide an overall picture of the financial health of supermarket companies:

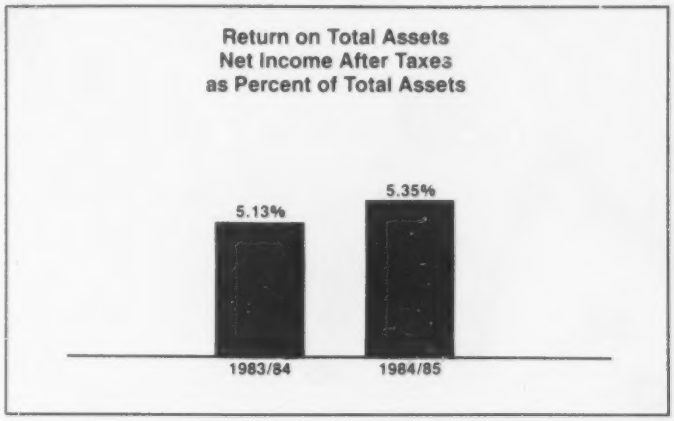
- profit margin
- return on total assets
- return on net worth

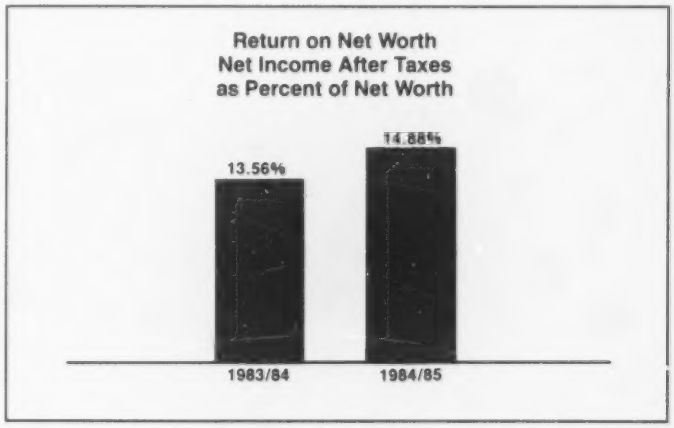
The profit margin is simply net income as a percentage of sales. It measures the portion of the firm's sales dollar that is left after paying all expenses, including the cost of the products. For the supermarket companies in 1984/85, the after tax profit margin was 1.15 percent.

Return on total assets is calculated by expressing net income as a percentage of total assets. It measures the ability of a company's combined equity and debt capital to generate profits. In 1984/85 supermarket companies' return on total assets increased to 5.35 percent from 5.13 percent one year earlier.

Return on net worth is calculated by expressing net income after taxes as a percentage of net worth. It reflects the earning power of the stockholders' equity in supermarket companies. Return on net worth for supermarket firms was 14.88 percent in 1984/85, up from 13.56 percent for the previous year.







KEY FINANCIAL RATIOS BY COMPANY SIZE

Profit ratios were calculated for three company size categories based on annual sales of:

- less than $50 million
- $50 to $500 million
- more than $500 million

On average, all three size categories improved their profitability in 1984/85 compared to 1983/84.

The largest firms had the highest average return on sales. The smallest companies showed the highest return on assets and net worth.

In the sample of companies included in this *Review*, 99 percent of the sales of small and medium sized companies were through supermarkets. Typically, the larger firms generated 90 percent of their revenues from supermarkets and 10 percent from other sources.

Profit Margin
Net Income After Taxes as a Percent of Sales

	1983/84	1984/85
Sales Under $50 Million	0.48%	0.78%
Sales Between $50 and $500 Million	0.81%	0.83%
Sales Over $500 Million	1.21%	1.36%

Return on Total Assets
Net Income After Taxes as a Percent of Total Assets

	1983/84	1984/85
Sales Under $50 Million	3.39%	5.86%
Sales Between $50 and $500 Million	4.12%	3.97%
Sales Over $500 Million	5.60%	5.75%

Return on Net Worth
Net Income After Taxes as a Percent of Net Worth

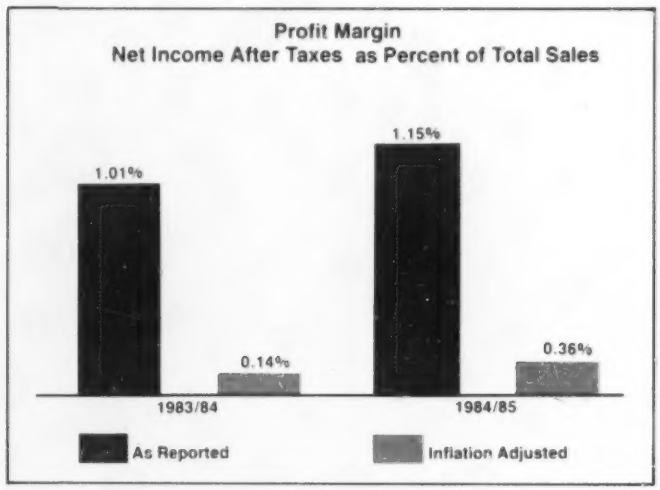
	1983/84	1984/85
Sales Under $50 Million	9.22%	16.35%
Sales Between $50 and $500 Million	10.89%	11.01%
Sales Over $500 Million	15.03%	15.64%

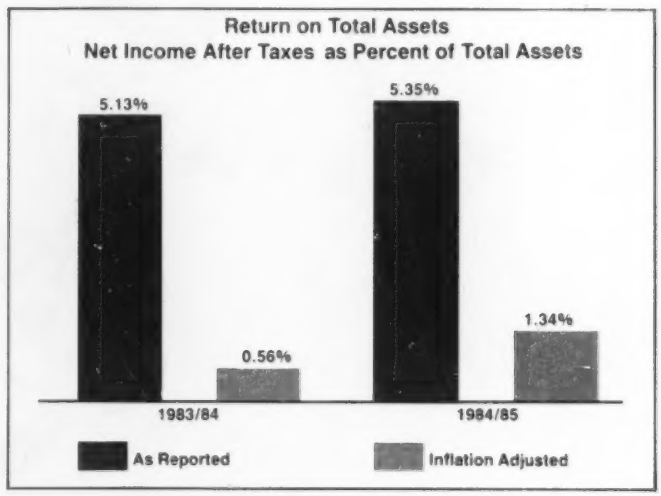
Key Financial Ratios Adjusted For Inflation

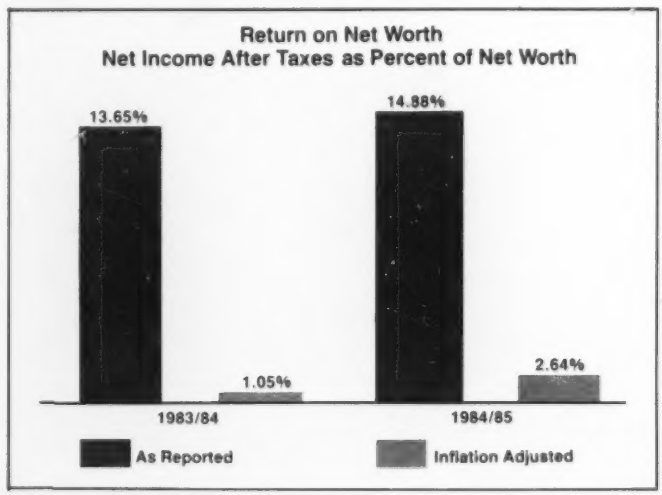
The performance measures discussed in the previous section are subject to distortion caused by inflation. For comparison, ratios are presented on an inflation-adjusted basis in order to more accurately reflect the economic well-being of supermarket firms.

The inflation adjustments used in the *Review* are those prescribed by Statement of Financial Accounting Standards No. 33. Such adjustments restate "cost of sales" and "depreciation" from the amounts recorded in historical dollars to current dollars. In so doing, (1) the impact of profits realized on inventory is removed from the income statement, and (2) the depreciation charge is increased to reflect the current costs of replacing assets.

Low inflation in 1983 and 1984 brought real growth to the supermarket industry. The inflation-adjusted ratios were only slightly positive for 1983/84 and 1984/85. The profit margin, return on total assets and return on net worth were 0.36 percent, 1.34 percent and 2.64 percent respectively for 1984/85.





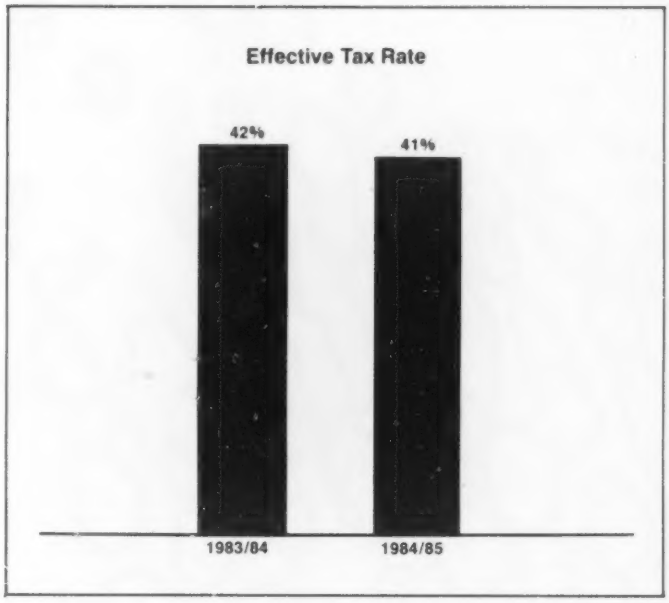


Tax Rates

Income Taxes

1984/85 income taxes paid by supermarket companies were 41 percent of pre-tax profits.

Income taxes affect corporations by consuming much, if not all, of their "real" pre-tax profits. Income tax calculations for an individual company are based upon net income calculated on a historic cost basis. For tax reporting, no adjustments are made to reflect the erosion of purchasing power that occurs through inflation. For example, depreciation expense for equipment is based on its actual cost, rather than on the current cost of replacing it.



Wage Taxes

In addition to taxes on income, supermarkets pay taxes based on wages. Company data are collected for FICA tax payments and Unemployment Compensation payments. In 1984/85, FICA tax payments amounted to 0.73 percent of sales. Unemployment Compensation payments were 0.17 percent of sales.

FINANCIAL STATEMENTS

Income Statement

The account balances in the income statement presented below have been expressed as percentages of sales.

Income Statement for Supermarket Companies
(In Percentages; Sales = 100%)

	1983/84	1984/85
Sales	100.00%	100.00%
Cost of Sales and Operating Expenses	98.20	98.12
Interest Expenses	0.46	0.52
Total Costs & Expenses	98.66	98.64
Operating Income	1.34	1.36
Other Income	0.36	0.43
Income Before Taxes	1.70	1.79
Total Taxes on Income	0.71	0.74
Extraordinary Items (Net)	0.02	0.10
NET INCOME	1.01	1.15

Balance Sheet

The account balances in the balance sheet presented below have been expressed as percentages of total assets.

End-of-Year Balance Sheet for Supermarket Companies
(In Percentages; Total Assets = 100%)

ASSETS	1983/84	1984/85
CURRENT ASSETS		
Cash	6.66	6.26
Accounts Receivable	4.33	4.24
Marketable Securities	2.78	3.35
Inventory (Note A)	31.47	31.66
Other Current Assets	3.64	2.94
Total Current Assets	48.88	48.45
PROPERTY & EQUIPMENT (Note B)		
Land	2.93	3.80
Buildings	21.85	21.62
Fixtures & Equipment	44.07	43.52
Leasehold Improvements	10.08	10.35
Total Property & Equipment	78.93	79.29
Reserves for Depreciation	(33.23)	(33.18)
Net Property & Equipment	45.70	46.11
OTHER ASSETS	5.42	5.44
TOTAL ASSETS	100.00%	100.00%

Note A: Some firms value at least part of their inventory on a LIFO (last-in, first-out) basis.

Note B: Property under capitalized leases is included in the appropriate property categories based on the type of property leased.

End-of-Year Balance Sheet for Supermarket Companies
(In Percentages; Total Liabilities = 100%)

LIABILITIES & NET WORTH	1983/84	1984/85
CURRENT LIABILITIES		
Notes Payable	2.12	2.17
Accounts Payable	22.68	22.39
Income Taxes Payable	1.35	1.19
Other Current Liabilities	10.40	10.18
Total Current Liabilities	36.55	35.93
LONG-TERM DEBT		
Mortgages	4.80	5.57
Bank Loans	4.67	6.78
Bonds & Debentures	2.72	2.54
Capitalized Lease Obligations	8.59	7.35
Other Noncurrent Liabilities	2.69	3.16
Total Long-Term Debt	23.47	25.40
DEFERRED LIABILITIES	2.48	1.81
Total Liabilities	62.50	63.14
NET WORTH		
Common Stock Outstanding or Proprietorship	4.19	3.62
Preferred Stock Outstanding	0.65	1.00
Paid-in Surplus	4.98	5.61
Retained Earnings	29.39	27.94
Treasury Stock	(1.71)	(1.31)
Total Net Worth	37.50	36.86
TOTAL LIABILITIES & NET WORTH	100.00%	100.00%

Historical vs. Inflation-Adjusted Balance Sheet Categories

Certain balance sheet categories were grouped and expressed as percentages of total assets, in both historical dollars and inflation-adjusted dollars. The most significant impact of the inflation adjustments was to restate (i.e. increase) the value of "net property and equipment" in current year dollars. (This increase was also added to "net worth.") These adjustments recognize that the current costs of replacing existing supermarket properties are significantly higher than the depreciated historic cost. Investors in supermarket properties are unable to realize those gains unless the company is dissolved or sold.

Balance Sheet Categories as Percent of Total—Historical Cost Basis

ASSETS	1983/84	1984/85
Inventory	35%	35%
Other Current Assets	17	16
Net Property & Equipment	43	44
Other Assets	5	5
Total	100%	100%
LIABILITIES AND TOTAL NET WORTH		
Current Liabilities	40%	39%
Long-Term Liabilities	25	26
Net Worth	35	35
Total	100%	100%

Balance Sheet Categories as Percent of Total—Adjusted for Inflation

ASSETS	1983/84	1984/85
Inventory	27%	27%
Other Current Assets	13	13
Net Property & Equipment	56	56
Other Assets	4	4
Total	100%	100%
LIABILITIES AND NET WORTH		
Current Liabilities	31%	30%
Long-Term Liabilities	20	21
Net Worth	49	49
Total	100%	100%

Inflation Adjustments

The Financial Accounting Standards Board (the "FASB") has recognized that financial statements prepared on the basis of historical costs may not be meaningful in times of rapid inflation. As a result, Statement of Financial Accounting Standards No. 33 requires large companies to present data which reflect the impact of inflation. One method prescribed in SFAS No. 33 is to adjust cost of sales and depreciation from the amounts recorded in historical dollars to current year dollars. This approach, called constant dollar accounting, removes the effect of inventory profits on cost of sales from the income statement, and increases the depreciation charge to amounts reflective of the current cost of replacing assets. The Consumer Price Index for All Urban Consumers is used to make such adjustments.

After adjusting for the effects of inflation on cost of sales and depreciation, supermarket companies achieved a slight profit in 1984/85 of 0.36 percent of sales.

Net Income for Supermarket Companies Adjusted for Inflation
(Expressed as a Percent of Sales)

	1983/84	1984/85
Net income, historic basis	1.12%	1.26%
Adjustments to reflect the impact of inflation on:		
Cost of sales	(.28)	(.31)
Depreciation	(.70)	(.59)
Net income adjusted for inflation and purchasing power	.14%	.36%

It is important, however, to consider one additional element during periods of inflation - gain or loss in purchasing power. In times of inflation, businesses that hold cash may be at a disadvantage in terms of general purchasing power because their cash will buy less at the end of the period than at the beginning. On the other hand, entities that have debts during inflationary periods may gain an advantage because their debts will be repaid with dollars of lower purchasing power. Statement of Financial Accounting Standards No. 33 requires that the net of these gains and losses be disclosed separately from income from continuing operations. This separate disclosure requirement reflects the FASB's concern that a company can gain from borrowing. (The FASB believed that a gain in purchasing power associated with debt is a sign of successful management only when the funds have been invested in assets that maintain their purchasing power.) As a result, the gains in purchasing power that the supermarket firms have realized on monetary items have not been reflected in the inflation-adjusted data that have been previously presented in this report. These data, however, have been included in the following table.

Net Income for Supermarket Companies Adjusted for Inflation (Expressed as a Percent of Sales)

	1983/84	1984/85
Net income, historic basis	1.12%	1.26%
Adjustments to reflect the impact of inflation on:		
Cost of sales	(.28)	(.31)
Depreciation	(.70)	(.59)
Purchasing Power	.34	.38
Net income adjusted for inflation and purchasing power	.48%	.74%

METHODOLOGY

Approach

The *Annual Financial Review* was developed from two primary sources of data: a survey mailed to the members of FMI and annual reports filed with the SEC on FORM 10-K.

For 1984/85, most of the financial data were supplied by the companies that responded to the survey. Data were not used for any company with sales of less than $2 million per store. Only firms with at least 50 percent of revenues from supermarkets were included in the sample.

Financial data for several large publicly traded companies were obtained from annual reports filed with SEC. In all, data were collected from 162 companies that operated 12,557 stores. These firms accounted for sales of $126 billion.

The firms were separated into two size categories based on annual sales - companies with less than $100 million, and companies with $100 million and over.

In order to develop the industry averages reported, means were calculated for each strata (size category) and were weighted using data from the 1982 Census of Retail Trade. The Census data are shown in the table below. The stratification and weighting of data help eliminate year-to-year changes that result from changes in the sample of firms submitting surveys.

We believe this method of developing average financial estimates for supermarket companies provides the best published measurement of trends in the supermarket industry's capital structure. It does not, however, totally eliminate the problems of changes in sample size, and varying fiscal year ends.

Supermarket Population Based on 1982 Census of Retail Trade*

Firm Sales (Millions)	% of Total Firms	1982 Sales (Millions)	% of Total Sales
Less than $100	97.4%	$ 57,792,633	30.25%
$100 and Over	2.6%	$133,268,115	69.75%
	100.0%	$191,060,748	100.00%

*Source: U.S. Census Bureau (latest available data)

APPENDIX

This year's *Review* was developed using a new methodology for data collection and for developing estimates. The Methodology section of this report explains the approach used.

Prior to this year, where firms operated both supermarkets and other related lines of business, the *Annual Financial Review* was based on estimates of the supermarket industry using data only from firms' supermarket operations. For a description of the methodology used see the *Annual Financial Review* for 1983 or earlier years.

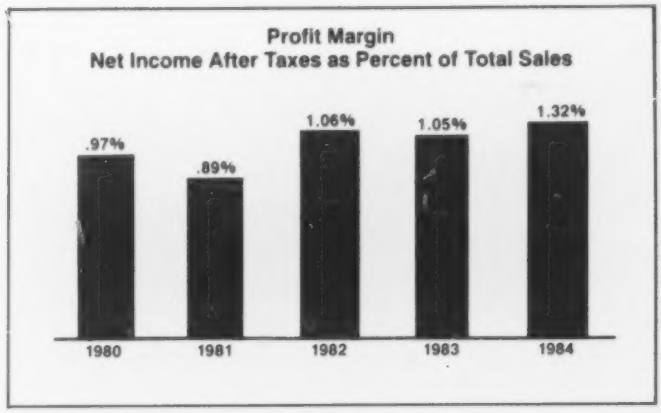
This appendix contains supermarket industry estimates for 1984 using the methodology employed in prior years. The estimates for 1984 were developed using the old methodology for comparability to prior years.

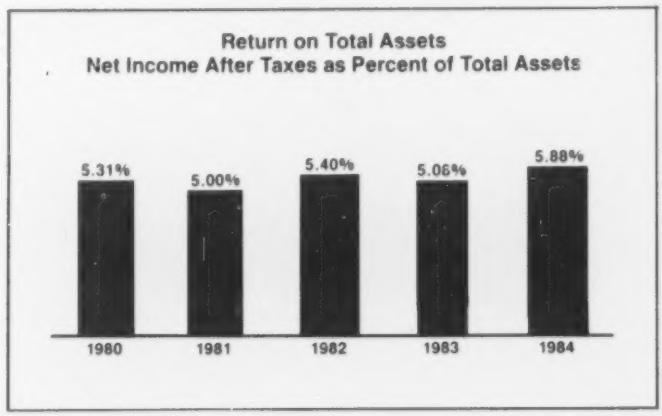
The estimates calculated with the old methodology and those calculated with the new methodology will differ. For example, using the old methodology, the net profit margin is 1.35 percent. With the new methodology the net profit margin is 1.15 percent.

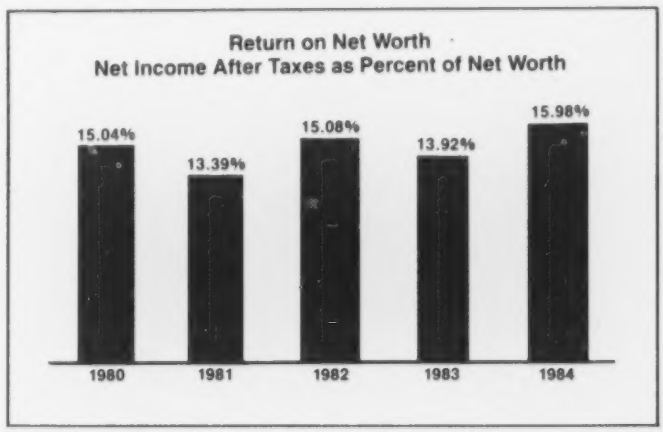
Some of the differences between the two sets of data occur because:

- The sample size for each is different. In this year's sample, because of the new methodology, we were able to include more companies, and larger companies.
- In previous years, inventory was adjusted for firms using LIFO. The inventory was converted back to FIFO. Under the new approach no adjustments are made in the inventories reported by the sample companies.
- The reporting time periods are different with the new methodology. In past years, surveys were accepted for fiscal years falling from January to December. This year the surveys had fiscal year ends that went from April to March.

In future years the *Review* will include estimates using the new methodology only.







Income Statement

The account balances in the income statement presented below have been expressed as percentages of sales, on a historic cost basis.

Income Statement for the Supermarket Industry
(In Percentages; Sales = 100%)

	1980	1981	1982	1983	1984
Sales	100.00%	100.00%	100.00%	100.00%	100.00%
Cost of Sales and Operating Expenses	98.20	98.62	98.24	98.23	97.89
Interest Expenses	.60	.51	.48	.46	.47
Total Costs & Expenses	98.80	99.13	98.72	98.69	98.36
Operating Income	1.20	.87	1.28	1.31	1.64
Other Income	.36	.55	.34	.42	.34
Income before Taxes	1.56	1.42	1.62	1.73	1.98
Total Taxes on Income	.55	.53	.57	.70	.79
Extraordinary Items (Net)	(.04)	—	.01	.02	.13
NET INCOME	.97%	.89%	1.06%	1.05%	1.32%

Balance Sheet

The account balances in the balance sheet presented below have been expressed as percentages of total assets, on a historic cost basis.

End-of-Year Balance Sheet for the Supermarket Industry
(In Percentages; Total Assets = 100%)

ASSETS	1980	1981	1982	1983	1984
CURRENT ASSETS					
Cash	6.86%	8.03%	7.10%	5.82%	6.83%
Accounts Receivable	3.65	4.12	3.80	4.13	4.76
Marketable Securities	3.13	2.72	3.26	2.56	2.59
Inventory (Note A)	35.26	35.10	33.29	34.66	35.08
Other Current Assets	3.31	2.53	4.38	4.00	3.37
Total Current Assets	52.21	52.50	51.83	51.17	52.63
PROPERTY & EQUIPMENT (Note B)					
Land	2.32	2.30	2.32	2.75	3.27
Buildings	21.86	14.43	18.78	21.09	17.54
Fixtures & Equipment	39.73	40.94	40.83	42.89	40.83
Leasehold Improvements	7.29	9.62	7.30	8.97	9.71
Total Property & Equipment	71.20	67.29	69.23	75.70	71.35
Reserves for Depreciation	(28.51)	(26.01)	(29.33)	(32.84)	(30.86)
Net Property & Equipment	42.69	41.28	39.90	42.86	40.49
OTHER ASSETS	5.10	6.22	8.27	5.97	6.88
TOTAL ASSETS	100.00%	100.00%	100.00%	100.00%	100.00%

Note A: Some firms value at least part of their inventory on a LIFO (last-in, first-out) basis. End-of-year inventories were recorded on a FIFO (first-in, first-out) basis for this report.

Note B: Property under capitalized leases is included in the appropriate property categories based on the type of property leased.

End-of-Year Balance Sheet for the Supermarket Industry
(In Percentages; Total Liabilities = 100%)

LIABILITIES & NET WORTH	1980	1981	1982	1983	1984
CURRENT LIABILITIES					
Notes Payable	2.39%	2.23%	3.16%	2.43%	2.77%
Accounts Payable	21.62	22.14	20.82	19.84	20.64
Income Taxes Payable	1.57	1.60	1.26	1.20	1.53
Other Current Liabilities	12.41	13.70	13.31	13.89	13.67
Total Current Liabilities	37.99	39.67	38.55	37.36	38.61
LONG-TERM DEBT					
Mortgages	6.50	3.81	5.38	4.57	3.55
Bank Loans	4.84	6.46	4.61	5.46	5.95
Bonds & Debentures	1.00	1.56	3.81	2.48	3.24
Capitalized Lease Obligations	9.37	6.83	7.50	7.86	5.79
Other Noncurrent Liabilities	2.75	3.14	3.00	2.53	2.52
Total Long-Term Debt	24.46	21.80	24.30	22.90	21.05
DEFERRED LIABILITIES	2.97	1.56	2.01	2.50	2.62
Total Liabilities	65.42	63.03	64.86	62.76	62.28
NET WORTH					
Common Stock Outstanding or Proprietorship	4.54	8.35	4.95	6.58	4.61
Preferred Stock Outstanding	.80	1.05	.96	.15	1.26
Paid-in Surplus	5.74	6.32	5.81	4.34	5.16
Retained Earnings	24.17	22.72	24.79	27.54	28.25
Treasury Stock	(.67)	(1.47)	(1.37)	(1.37)	(1.56)
Total Net Worth	34.58	36.97	35.14	37.24	37.72
TOTAL LIABILITIES & NET WORTH	100.00%	100.00%	100.00%	100.00%	100.00%

Definitions

Balance Sheet Captions

INVENTORY includes all goods held for sales by supermarket companies.

OTHER CURRENT ASSETS include all assets (except inventory) with a defined life of less than one year (e.g., cash, accounts receivable, prepaid expenses, short-term investments, etc.).

NET PROPERTY & EQUIPMENT is all property, plant and equipment, including capital leases, less accumulated depreciation and amortization.

OTHER ASSETS include all assets (except property and equipment) with a defined life greater than one year (e.g., investments in other companies, long-term receivables, etc.).

CURRENT LIABILITIES include all debts and expenses which are due within one year (e.g., accounts payable, accrued liabilities, current portions of long-term debt, etc.).

LONG-TERM LIABILITIES include all debts and expenses which are due after one year (e.g., long-term debt, capital lease obligations, deferred taxes, etc.).

NET WORTH is merely the difference between total assets and total liabilities. It is typically comprised of stock, paid-in-surplus, retained earnings and treasury stock.

Income Statement Captions

SALES represent all sales reported by supermarket companies.

COST OF SALES AND OPERATING EXPENSES include the cost of merchandise sold by supermarkets plus all the other expenses of operating the stores, distribution facilities, and the central office.

INTEREST EXPENSE includes all interest charged on short- or long-term debt and on capital lease obligations.

OTHER INCOME includes all non-operating income (e.g., interest income, gain on sale of securities, etc.).

TOTAL TAXES ON INCOME are the Federal and state taxes imposed on the supermarket companies which are based on net income as reported to the government.

EXTRAORDINARY ITEMS include all items which occur infrequently and are unusual in nature (e.g., provisions for the disposition of facilities, realization of tax loss carry forwards, etc.).

Ratios

PROFIT MARGIN is the ratio of net income to sales.

RETURN ON TOTAL ASSETS is the ratio of net income to total assets.

RETURN ON NET WORTH is the ratio of net income to net worth.

Inflation Adjustments

INFLATION ADJUSTED NET INCOME is equal to net income as reported in historical dollars, less "constant dollar" adjustments to reflect the impact of inflation on (1) cost of sales (i.e., to remove the effect of inventory profits from cost of sales), and (2) depreciation (i.e., to increase the depreciation charge to reflect the current cost of replacing assets).

CONSTANT DOLLAR ACCOUNTING is a method of reporting financial elements in dollars which have the same general purchasing power.

MONETARY ITEMS are assets or liabilities which will be realized or paid for in cash for the exact amount of the amounts recorded on the balance sheet.

NON-MONETARY ITEMS are assets or liabilities which cannot be converted directly to cash for the amount recorded on the balance sheet (e.g., inventory, property and equipment, deferred credits, etc.).

PURCHASING POWER GAIN OR LOSS is found by restating in constant dollars the (1) opening and closing balance of monetary assets and liabilities, and (2) transactions in monetary assets and liabilities.